

# NJ Review & Economic Outlook for 2002-2003

**Forecast Summary: "After the damages of recession and the shocks of terrorism, there will be a modest recovery in jobs, income and investment in the 2<sup>nd</sup> half of 2002"**

*Joseph J. Seneca, Chairman*

## NJ Forecast 2002-03 .....



Although 2001 ended with fewer jobs, higher unemployment and much slower growth in retail spending compared to a year earlier, the 2001 recession appears to be mild and likely of average duration. The 2002-03 outlook for NJ is based on a flat 1<sup>st</sup> half 2002 followed by a modest paced recovery.

Summary: New Jersey Forecast (% Chg)		
	2002	2003
Gross State Product (Current \$)	2.2%	4.5%
Personal Income (Current \$)	2.0%	4.8%
Retail Sales (Current \$)	1.4%	5.1%
Consumer Price Index (All Urban)	2.0%	2.2%
Total Non-Ag Employment	0.2%	1.0%

The forecast is for Gross State Product to advance 2.2% and 4.5% in 2002 and 03. Inflation remains stable at, or near, 2%. Personal income growth lags GSP at 2.0% in 2002, but wage gains in 2003 boost personal income by 4.8%. Retail spending adds only 1.4% in 2002, but recovers with a +5% increase in 2003.

For 2002, employment recovers slowly with a gain of fewer than 10 thousand jobs. As the recovery broadens in 2003, employment growth accelerates, led by improvements in selected growth industries (clusters), for a gain of about 40 thousand jobs. Despite those job gains, an expanding labor force holds the unemployment rate near the 5% level.

Among the US-wide factors contributing to this outlook are a continuation of low interest rates, low inflation, low energy prices, increased federal spending (security and defense), and scheduled reductions in federal tax rates.

A number of regional/local factors were factored into the New Jersey forecast. On a positive side is the absence of excesses, such as high office vacancy rates and stocks of unsold homes. The forecast anticipates a return to above average growth for the State's growth industries (clusters) led by pharmaceutical (healthcare) businesses. Also, the Outlook anticipates sectors related to safety and security to outperform the general economy.

The US capital goods sector, which accounted for much of the Nation's decline in industrial production and is underrepresented in New Jersey, should not restrain a mid-2002 recovery. We have not assumed a post-September 11<sup>th</sup> federal stimulus in this forecast. That, in addition to increased defense spending and contracting expenditures should increase the likelihood of a recovery of the State's economy in 2002-03.

The likelihood of the recovery being a modest one at best is reinforced by a much-weakened New York City economy that typically exerts a strong influx on Northern NJ businesses. Current forecasts by NYC officials anticipate an extended period weaker in the City's tourism business, financial businesses and all consumer-related sectors during this forecast period. Another weak sector is foreign trade. The strong dollar and economic weakness of our major trading partners imply that we cannot expect any significant growth in the State's \$20+ billion export sector.

## The US Economy.....



March 2001 marked the end of a record 10-year expansion and was the start of the 10<sup>th</sup> recession since WWII commenced. This recession was marked by sharp declines in industrial production and sales that weakened nearly all regions of the US.

Almost all factory sectors have declined, especially capital goods, technology and aircraft. Large declines in communications equipment impacted New Jersey disproportionately, but modest gains in pharmaceuticals partially offset these losses.

Despite nine months of recession, **consumer spending** actually increased throughout 2001, albeit at lower rates of growth. Low inflation, low cost financing, tax rebates, mortgage refinancing and a modestly healthy labor market combined to support consumer spending. NJ benefited from surging outlays for consumer durables (autos), spurred by zero or low cost dealer financing. Expenditures for energy and utilities declined as lower fuel prices and moderate weather combined to ease expenditures. Later in 2001 spending fell sharply on transportation and recreation.

**Residential real estate** displayed little change in 2001 from very high levels of sales and home starts, as declining mortgage rates made homes more affordable. The **commercial real estate** sector weakened during the year following the demise of start-up dot.coms, downsizing at manufacturers and capital goods producers. Increasing vacancy rates and softening rental rates were typical in most regions.

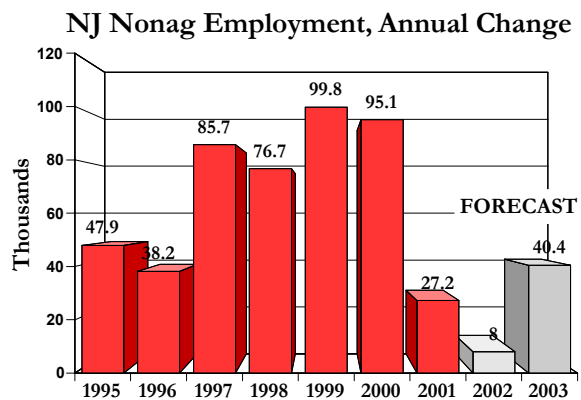
**Labor markets** continued to ease during the year with the 4<sup>th</sup> quarter US unemployment rate at 5.6%, up from 4.0% one year ago. Most job losses were in manufacturing and transportation. Services recorded a small decline led by losses in temporary help services.

**Other States.** The 2001 recession is a broad-based national recession that has impacted each region and most states. Employment declined on a month-to-month basis in all regions and jobless rates are rising. States with the largest number of lost jobs in 2001 were geographically diverse - led by Georgia, New York and Indiana. Many states found hospitality and tourism sectors suffered badly from the slowing economy and the impact on air travel from the terrorist attacks.

## N.J. Employment.....

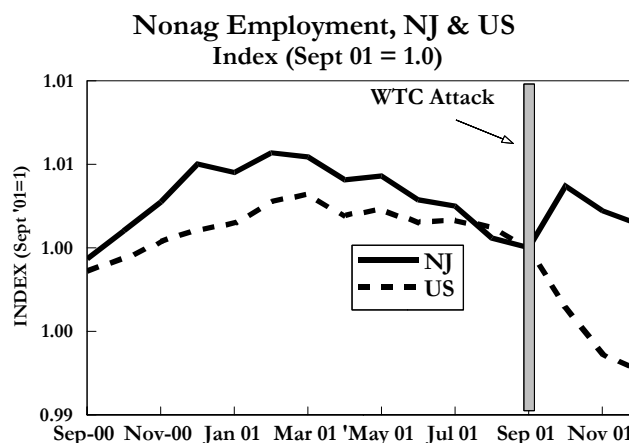


Despite the onset of recession, NJ employment for 2001 was 27,200 above the 12-month average for 2000. This resulted from strong year-over-year growth in early 2001. From February through December, New Jersey lost 17,200 jobs. Averaging almost 100 thousand net new jobs in 1999 and 2000, the 01 job market was the weakest since 1992.



**By the end of 2001**, the State's labor market reflected the aftereffects of the national recession and mixed impacts from the WTC attack. On a monthly basis, jobs peaked in February at 4,033,800 and then paralleled national declines in employment. After the September 11<sup>th</sup> terrorist attacks, the State added jobs in October as displaced NYC businesses scrambled to locate temporary or new permanent operations in NJ. By December, several large financial/brokerage companies moved employees back to Manhattan, leaving NJ with a net gain of about 9,000 financial jobs since the September WTC attacks.

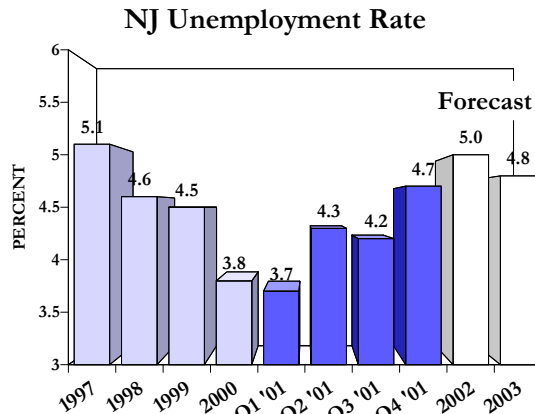
From February to December the effect of relocating employers left NJ with a net decline of 17,200, a considerably smaller loss than what would have occurred if not for the temporary relocation of NYC jobs.



The NJ unemployment rate climbed during 2001, rising to an average rate of 4.7% in the 4<sup>th</sup> quarter reflecting weakened labor market conditions and significant air transportation sector layoffs. Despite the combination of

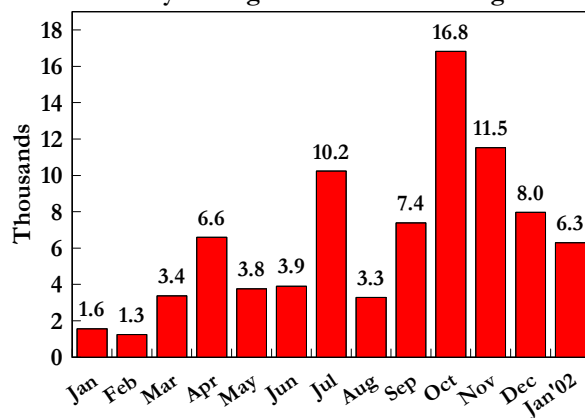


a weak US economy and significant regional disruptions, the NJ rate remained well below the US rate of 5.6% for the fourth quarter. The NJ unemployment rate has been at or below the national average since January 2000.



Initial claims for unemployment insurance, a leading indicator of job layoffs, began to increase in March 2001. Claims peaked in October following the WTC attacks and have since trended downward suggesting that the deterioration in NJ labor markets may be abating.

**NJ Initial Claims for Unemployment Insurance**  
Monthly Average Year-to-Year Change

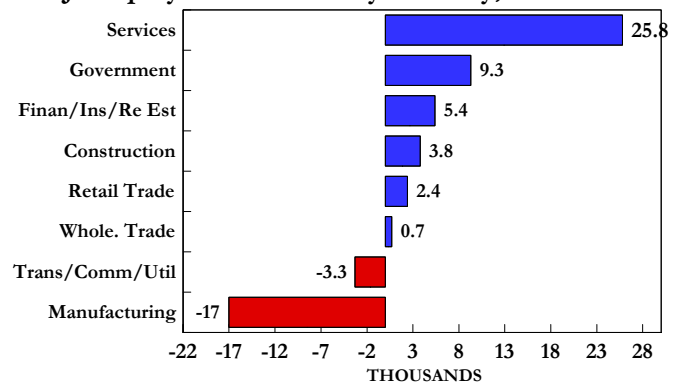


Looking forward, NJ employment is expected to stabilize in the 1<sup>st</sup> half of 2002, with annual average employment to remain slightly above the 2001 level. Although the forecast for 2003 is for a continuing modest job recovery of about 1%, the unemployment rate will continue to rise for some time. The unemployment rate should average 5% in 2002, and decline slowly to 4.8% in 2003.

## Employment By Industry .....

Employment change for 2001 was the net result of two distinctly different labor markets in NJ. The State's job losses were almost entirely in the manufacturing sector. Factory jobs fell by 17 thousand, or -3.7%, compared to average levels in 2000. Services, on the other hand, continued the long-term growth trend, with a gain of 25,800 over the year. Again, these changes are based on yearly averages. From February to December, service employment added only 6,700 jobs, or .5%.

**NJ Employment Growth by Industry, 2000-2001**



While employment in most non-manufacturing sectors was growing in early 2001, the national and State economic slowdown spread to most industry sectors. By year-end, only three industry sectors; government, finance, and services, saw job gains from the February 2001 employment peak to December.

The finance/insurance/real estate industry job gain was related to the relocation of NYC financial firms mentioned earlier in this report. Government gains were attributable to increased hiring for local education and the temporary relocation of over 2,000 Port Authority of NY-NJ employees from NYC to NJ following September 11th.



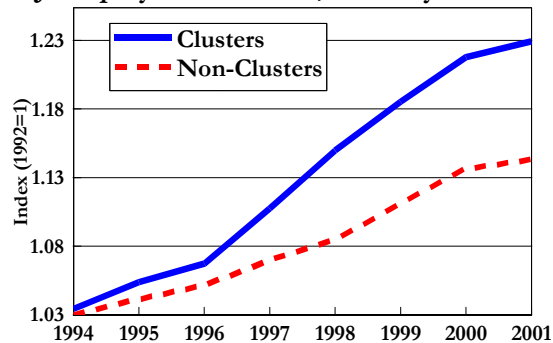
## Industry Clusters...

New Jersey's employment growth during the 1990's was concentrated in six well-defined business clusters of economic activity - 1. information technology (IT), 2. research & technology services, 3. pharmaceuticals, 4. finance, 5. logistics, and 6. casino & entertainment.

Each cluster includes groups of interrelated industries that are characterized by competitiveness and innovation. These clusters were defined to identify producers of high value products and services that support high wage jobs. Therefore, NJ cluster industries are key to the State's outlook and overall economic health.

**NJ growth clusters**, which accounted for a disproportionate share of NJ job growth over the economic expansion of the 1990's, continued to lead even as overall growth slowed in 2001. Only 30% of the State's payroll jobs are in the six clusters, but they accounted for nearly 40% of total job growth this year. The "clusters" growth rate was about 1.0% year over year, versus non-cluster growth of 0.6%.

**NJ Employment Growth, Industry Clusters**



The gains were led by finance/insurance (2.8%) and research & technology services (1.8%).

**NJ Employment Growth by Industry Cluster, 2000-2001**

	Number (000)	Percent
Finance Cluster	5.0	2.8%
Research & Tech. Cluster	2.6	1.8%
Pharma/BioTech Cluster	1.2	1.1%
Casino/Entertainment Cluster	1.2	1.0%
Logistics Cluster	2.0	0.5%
Information Tech. Cluster	-1.7	-0.8%
Cluster Total	10.3	1.0%
Total Non-Clusters	17.0	0.6%

## The Outlook by cluster -

**Finance** - It is too soon to assess the long-term impact of recent moves from NYC, but the weak equity markets in 2001 will continue to depress personal income gains and employment in this sector. Longer term, financial services should remain among the State's fastest growing and highest paying sectors.

**Research & technology services** cluster, which includes service industries such as, engineering, accounting, and testing laboratories, serves a broad national and international market and has experienced little negative impact by aggregate economic conditions and the WTC attack.

**Pharmaceuticals'** output and employment, which does not closely follow the economy's cyclical patterns, should maintain its current levels of strength for New Jersey. In addition, industry demand will continue to increase due to the demographics of an aging population. Also, the aftereffects of 9/11 has led to increased demand for vaccines and other medical products to combat the threat of bio-terrorism.

**Casino & entertainment** - Atlantic City casinos attracted fewer visitors in the period immediately after 9/11, but preliminary data for December showed a dramatic 18% increase in revenues over December 2000. The amusement sector also showed strong job growth during the summer 2001 season.

**Logistics** includes the movement and distribution of goods and passengers in the State. Air transportation declined after 9/11 as the number of flights were curtailed. The volume of goods moved will adjust to slowing overall economic conditions. However, the employment in the logistics sector has remained fairly steady in the face of the recent slowdown.

The **information technology** cluster experienced declines in 2001 stemming from the national reduction in technology capital spending. The long term restructuring in telecommunications has also cost jobs nationwide, and especially in NJ.

## Personal Income & Retail Spending.....



NJ personal income advanced by an estimated 5.2% in 2001, slightly ahead of the 5% US average. Wages & salaries, the largest component of income jumped by almost 6%, reflecting tight labor market conditions that existed early in the year. Overall personal income growth was restrained by slower growth in investment incomes and small business incomes (proprietor's income).

For 2002, personal income grows about 2%, constrained by sluggish job growth, lower bonuses in the finance sector, and only modest wage increases elsewhere.

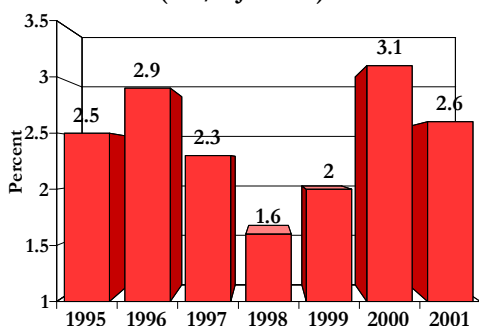
For 2001, retail sales were rocked by a slowing economy, a drop in home building, the WTC attacks, and a late season drop in tourism, but were then helped by year-end sales promotions for autos. Overall sales likely increased 4 to 6% last year. The forecast for only a modest recovery and an uncertain outlook for tourism and gaming dampens the retail recovery and limits gains to 1 to 2% in 2002, but increasing to 5% in 2003.

## Consumer Prices.....



Regional prices were rising steadily through 2000 when energy costs pushed the NY/NJ CPI to a 3.1% annual increase, the sharpest rise since 1992. A slowing economy and sharp energy disinflation in 2001 held the rise in consumer prices to 2.6%, providing an unexpected boost to consumer's real income.

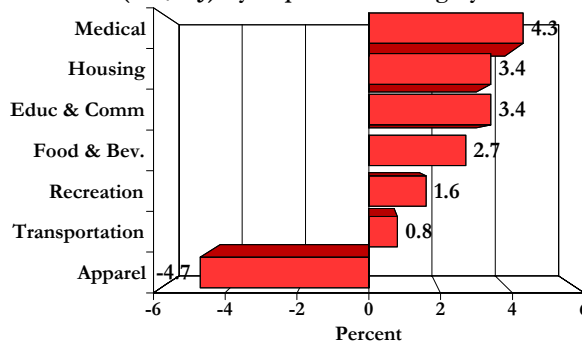
**Consumer Price Index, Annual Rate  
(NY/NJ PMSA)**



Contributing factors to moderating inflation were the drop in oil from over \$30 per barrel a year ago to under \$20 currently, the strong US dollar combined with excess global capacity that pushed down import prices

for many consumer and producer products, and retailers who engaged in heavy price discounting and cut-rate financing to draw consumers into stores through the end of 2001.

**Consumer Price Index, Annual Rate  
(NY/NJ) By Expenditure Category**



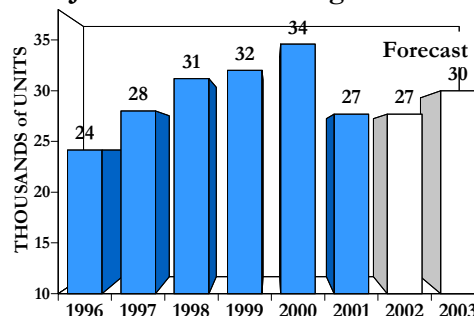
Despite the onset of recession, the cost of medical care, housing, and education/communication posted above average increases of 4.3% and 3.4%, and 3.4%, respectively. Food items rose 2.7%, while prices for recreation 1.6%, and transportation .8%, had below average increases. Prices for apparel in the region declined almost 5%.

## Investing in New Jersey .....



Residential building permits declined by an estimated 20% in 2001, returning to the mid-20 thousand range after three years of permits in excess of 30,000 and the decade high 34,000 new dwelling units authorized in 2000.

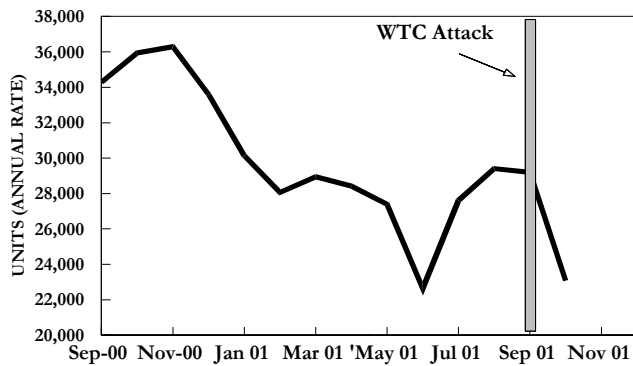
**NJ Residential Building Permits**



The decrease in NJ residential permits was related to the economic slowdown exacerbated by the WTC attack, which affected jobs, incomes and consumer confidence. Home prices, however, remained firm with a year over year average gain of 10%.



## NJ Residential Permits Seasonally Adjusted, Annual Rate

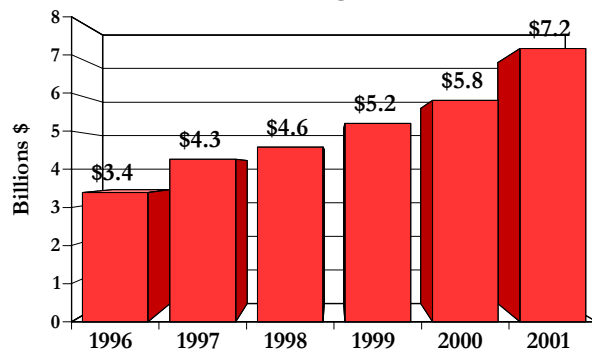


The outlook calls for housing permits to stabilize during the year at an annual rate close to the 2001 level of 27,700 units.

Although new home construction in NJ will be restrained by the scarcity and cost of buildable land, the State's demographics - including relatively low rates of new household formation and uncertain rates of future in-migration, lead to a recovery in 2003, boosting housing permits to 30,000 units.

**Total nonresidential building permits** are estimated to exceed \$7 billion in 2001, an increase of over 20% from 2000. Office buildings, the largest construction subcategory, accounted for 42% of non-residential permits. Planned office space for 20 million sq. feet, if completed, would add almost 10% to the total inventory of NJ office space. Nearly 60% of all planned new office space is in four counties; Somerset, Middlesex, Monmouth, and Hudson (with Jersey City accounting for more than 25% of the State total).

## NJ Non-residential Building Permits, Billions \$



Increased office construction that coincided with a slowing demand for office space pushed vacancy rates to the 12-13% range by the 3<sup>rd</sup> quarter of 2001. The upward trend in vacancy rates is expected to put downward pressure on asking rents, and possibly delay or cancel some planned construction.

Commercial and retail construction permits increased about 15% in 2001. Over one-half of the planned new space is in four NJ counties; Monmouth, Morris, Middlesex, and Union.

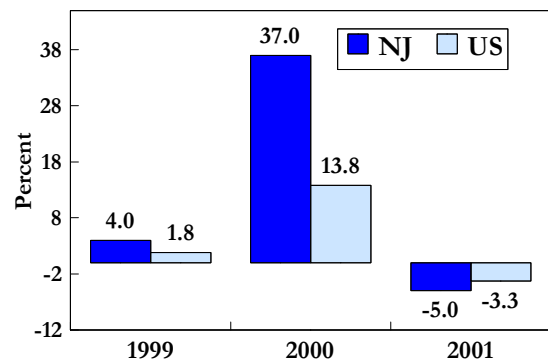
In 2001, construction of educational facilities was only 13% of total non-residential permits. For 2002 and 03 spending for the multi-billion dollar public school reconstruction and construction program will accelerate and contribute to the State's economic recovery.



## International Trade .....

Since international trade reflects market conditions in both trading partners, a deteriorating economic environment spreads quickly. For 2001, US exports fell 3.3% while New Jersey shipments declined by 5%. The declines followed a year (2000) in which US exports rose 13% and NJ shipments grew by a remarkable 37%.

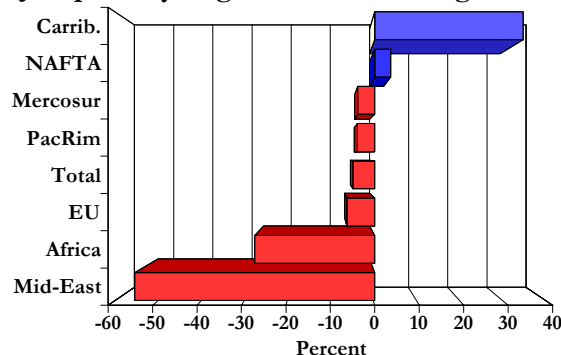
## Annual Growth in Exports- NJ & US, 1999-2001



Exporting offered little help to New Jersey manufacturers facing weak domestic markets in 2001. The decline in overseas trade was broad-based including: technology products (computer & electronic goods -15%), transportation equipment -27%, capital goods (machinery -6%, fabricated metals -26%) and consumer products (beverages -46%, apparel -23%, furniture -5%). Exports improved for food, +21%, printing & publishing, +19%, and second-hand goods, +69%.

Geographically, NJ exports increased to the Caribbean, (+33%) and to NAFTA (+4%), led by a strong 12% increase in sales to Mexico.

#### NJ Exports by Region, Percent Change 2000-01

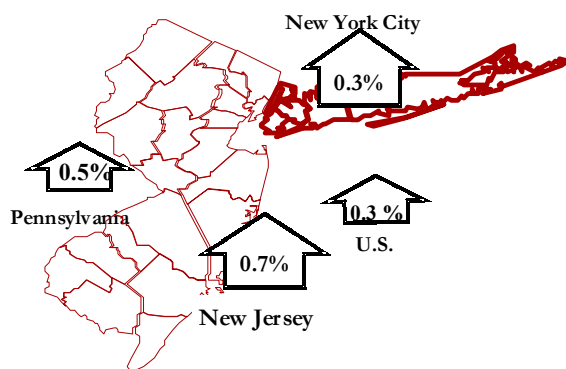


Exports declined on a year over year basis to the European Union (-6%), PacRim (-4%, with significant declines in shipments to China and Singapore), and the Mid-East (-54%). Sharply lower sales to Israel and Saudia Arabia headed the Mid-East's drop in NJ exports.

#### The Region

New Jersey fared slightly better than the nation and our regional neighbors in 2001. On an annual average basis, NJ employment growth of 0.7% was above the US average of 0.3%, Pennsylvania's 0.5%, and New York State's 0.6% rate.

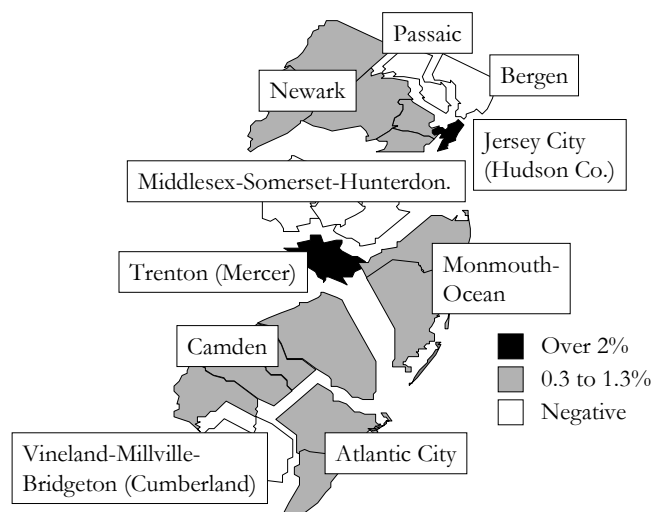
#### Non-Ag Employment, Percent Change 2000-01



New York City's labor market, which had been a driving engine for NJ, lost almost 100,000 jobs from December 00 to December 2001. Financial services, tourism and consumer industries were particularly hard hit.

#### NJ Labor Markets

The **Trenton** (Mercer County) and **Jersey City** (Hudson County) labor market areas experienced the highest employment growth rates in 2001, 2.6% and 2.7%. The Trenton/Mercer area growth can be largely attributed to the staffing of the new Merrill Lynch facility. Meanwhile, Jersey City continued to be the favored destination of New York City financial firms moving or expanding.



The five-county **Newark** labor area added the most jobs, 8,100 over the year, a rate of 0.8%, slightly above the Statewide average of 0.7%.

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## New Jersey Review & Economic Outlook: 2002 - 2003

	Forecast							
<i>(Current \$ or Nos.)</i>	1996	1997	1998	1999	2000	2001	2002	2003
Gross State Product (bill)	\$279.2	\$294.1	\$319.2	\$335.5	\$355.6	\$372.7	\$ 380.9	398.2
Personal Income (bill)	\$247.4	\$260.7	\$278.3	\$291.5	\$311.2	\$327.5	\$ 334.0	350.2
Retail Sales (bill)	\$76.2	\$81.9	\$86.0	\$94.0	\$101.9	\$106.0	\$ 107.5	113.0
New Vehicle Registrations (000's)	533.1	537.6	550.6	582.5	663.5	641.9	599.3	600.0
Non-Resident.Contracts (mill \$)	\$2,962	\$3,618	\$4,098	\$4,670	\$5,230	\$5,162	\$ 4,650	4883.0
Residential Building Permits (No.)	24,200	28,020	31,200	32,000	34,584	27,700	27,700	30,000
Consumer Price Index (All Urban)	111.3	113.9	115.7	117.9	121.6	124.7	127.2	130.0
<i>(Real 1992\$)</i>								
Gross State Product (bill)	\$250.9	\$258.2	\$275.9	\$284.5	\$292.4	\$298.8	\$299.5	\$306.3
Personal Income (bill)	\$222.3	\$228.9	\$240.5	\$247.2	\$255.9	\$262.6	\$262.6	\$269.4
Retail Sales (bill)	\$68.5	\$71.9	\$74.3	\$79.7	\$83.8	\$85.0	\$84.5	\$86.9
Non-Resident.Contracts (mill)	\$2,660.9	\$3,176.5	\$3,541.9	\$3,961.0	\$4,301.0	\$4,138.7	\$3,655.8	\$3,756.4
Employment:								
Total Non-Farm (000)	3,638.90	3,724.60	3,800.80	3,866.1	3,996.2	4,023.4	4,031.4	4071.8
Manufacturing (000)	483.5	481.9	478.0	466.5	462.4	445.4	429.8	416.9
Service Producing Industries (000)	2,458.80	2,539.8	2,615.5	2,688.7	2,786.6	2,818.0	2,833.2	2878.0
Government	570.6	570.3	571.7	577.6	588.8	598.1	604.08	607.1
Unemployment Rate (%)	6.2%	5.1%	4.6%	4.6%	3.8%	4.2%	5.0%	4.8%
<b>Percent Change from previous year:</b>								
	<b>1996</b>	<b>1997</b>	<b>1998</b>	<b>1999</b>	<b>2000</b>	<b>2001</b>	<b>Forecast</b>	
							<b>2002</b>	<b>2003</b>
Gross State Product (Current \$, bill)	3.9%	5.4%	8.5%	5.1%	6.0%	4.8%	2.2%	4.5%
Personal Income (Current \$, bill)	4.9%	5.3%	6.8%	4.7%	6.8%	5.2%	2.0%	4.8%
Retail Sales (Current \$, bill)	3.7%	7.5%	5.0%	9.3%	8.4%	4.0%	1.4%	5.1%
New Vehicle Registrations	4.8%	0.8%	2.4%	5.8%	13.9%	-3.3%	-6.6%	0.1%
Non-Resident Contracts (Current \$, r	6.9%	21.4%	13.3%	14.0%	12.0%	-1.3%	-9.9%	5.0%
Residential Building Permits (No.)	12.6%	15.9%	11.3%	2.6%	8.1%	-19.9%	0.0%	8.3%
Consumer Price Index (All Urban)	2.9%	2.4%	1.6%	1.9%	3.1%	2.6%	2.0%	2.2%
Gross State Product (92\$, bill)	1.9%	3.2%	6.9%	3.1%	2.8%	2.2%	0.2%	2.3%
Personal Income (92\$, bill)	1.8%	3.4%	5.1%	2.8%	3.5%	2.6%	0.0%	2.6%
Retail Sales (92\$, bill)	0.8%	5.1%	3.4%	7.3%	5.1%	1.4%	-0.6%	2.9%
Non-Resident Contracts (92\$, mill)	3.9%	18.6%	11.5%	11.8%	8.6%	-3.8%	-11.7%	2.8%
Employment:								
Total Non-Farm (000)	1.1%	2.4%	2.0%	1.7%	3.4%	0.7%	0.2%	1.0%
Manufacturing (000)	-2.8%	-0.7%	-0.8%	-2.4%	-0.9%	-3.7%	-3.5%	-3.0%
Service Producing Industries (000)	2.1%	3.3%	3.0%	2.8%	3.6%	1.1%	0.5%	1.6%
Government	-0.5%	-0.1%	0.2%	1.0%	1.9%	1.6%	1.0%	0.5%